Alberta Capital Finance Authority

2007
Annual Report

ACFA
ALBERTA CAPITAL FINANCE AUTHORITY

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DIRECTORS

BOARD OF DIRECTORS

Appointed

C.F. Barth
R. Bhatia
F.W. Clarke
L.R. Gordon
S. Ewart-Johnson

Elected

L. Walker	- Representing Class B shareholders
E.A. Gibbons	- Representing Class C shareholders
Vacant	- Representing Class D shareholders
D.O. Lussier	- Representing Class E shareholders

AUDIT COMMITTEE

C.F. Barth	- Chair of the Audit Committee
H.N. Johnsrude	- Member
L. Walker	- Member

OFFICERS

D.O. Lussier	- Chair of the Board
L.R. Gordon	- Vice-Chair
T.S. Stroich	- President and Treasurer
L. Epp	- Vice-President
J. Hui	- Corporate Secretary and Assistant Treasurer

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ORGANIZATION

Mission

To provide local authorities within the Province with flexible funding for capital projects at the lowest possible cost, consistent with the viability of the Alberta Capital Finance Authority.

Authority

The Alberta Capital Finance Authority is a non-profit Authority established in 1956 under the authority of the *Alberta Capital Finance Authority Act*, Chapter A-14.5, Revised Statutes of Alberta 2000, as amended.

Shareholders

The authorized stock of the Authority consists of the following shares with a par value of $10 each:

- 4,500 Class A, available only to the Crown
- 1,000 Class B, available only to municipal authorities (defined as including improvement districts, metis settlements, municipal districts, counties, special areas, and specialized municipalities) and to regional authorities (includes drainage districts, irrigation districts, regional airport authorities and regional services commissions), and health authorities (includes approved hospitals, mental health hospitals, regional health authorities, and provincial health boards)
- 750 Class C, available only to cities
- 750 Class D, available only to towns and villages
- 500 Class E, available only to educational authorities (includes school districts and divisions, colleges, technical institutes, universities and Northland School Division)

The business of the Authority is administered by a Board of Directors. The Lieutenant Governor in Council appoints up to five directors to represent the Class A common shareholder. Each of the other four classes of shareholders elects one director to the Board.

Loans

Maximum terms of loans for various projects are prescribed in the Authority's resolution relating to the terms and conditions for lending money to shareholders.

Financing

The Authority issues various debt obligations to obtain the funds necessary to finance loan requirements. These obligations of the Authority carry the unconditional guarantee of the Province of Alberta.

Chair's Report

February 14, 2008

It is my privilege and pleasure to present the Annual Report of the Alberta Capital Finance Authority for the year ended December 31, 2007, and to review its activities over the past year.

This past year was again one of growth and change for the Authority. 2007 saw over $1.240 billion in new loans, the highest on record and the second year in a row where over $1 billion in loans were issued. Over the past 10 years, since 1998, loans issued have increased from $160 million to $1.240 billion, seven times the volume and a 100% increase since 2004. Increasing population growth, renewal of aging infrastructure and the staggering increases in costs of capital construction has driven the need for increases in borrowing. Yet, even with this increased level of activities, debt and debt service levels remain relatively stable for most borrowers and credit rating agencies have given a AA+ rating to both major cities.

The Authority continues to adapt to our shareholders needs and in December 2007, issued our first 40-year loan. Although this term falls beyond our current term limits, the Board approved the increased term while determining that security for the loan can be maintained over this longer term. Based on early estimates received from our shareholders, 2008 and beyond should continue to show a high level of loan demand as our shareholders struggle to meet the needs for renewal and new infrastructure.

As noted last year, when loan demand in the early 1980's reached record levels, interest rates were at their highest nearly 19%, while in 2006 and again in 2007, rates remained historically low. The credit crunch has had an impact on our rates as although there was a more significant decline in Canadian Government Bond rates from June onward, the difference between ACFA rates and the Government of Canada rate for similar terms, increased significantly. In fact, ACFA, with the Province's guarantee, could borrow at about 24.5 basis points over Government of Canada rate for a 10 year term in January but by the end of the year, these spreads had increased to 44 basis points. These increasing spreads have meant that ACFA's own loan rates have not decreased as much as the Government of Canada's rates.

The increase in loan demand necessitated a significant increase in borrowing to fund this demand. ACFA issued new debt of over $1.55 billion of which $542 million was in short term debt which was repaid, except for $40 million, by year end. ACFA redeemed $335 million in bonds from Canada Pension Plan Investment Fund but borrowed a further $190.4 million from the Canada Pension Plan Investment Board. The balance of the funds, over $800 million were borrowed in the public market.

The Authority's goal is to operate on a break-even basis while maintaining a minimum yet positive level of retained earnings.

In 2007, the Authority approved the change to accounting policies from a cost basis to a full fair value basis which increased our retained earnings to $81.8 million. The change to fair value accounting adds the potential for greater volatility to future reporting periods as changes in the fair value of loans, debt and related derivative financial instruments will be measured and recorded in the financial statements.

Income for 2007 was $5.2 million before unrealized gains and losses from changing market values of our loans, debts and derivatives. An adjustment of $57.7 million (unrealized gains) was made to retained earnings on January 1, 2007 to account for the change to fair value accounting.

In 2007, Lorne Mann, who represented the Class "D" shareholders resigned from the Board in September and was not replaced as his election was scheduled for March 2008. I'd like to thank Lorne for his support over the past 2-1/2 years and his efforts on behalf of shareholders. Lawrence Gordon was reappointed for another three year term and was reappointed by the Minister of Finance as Vice Chair, and I was re-elected for a final three year term as the Class "E" shareholder representative. I wish to thank the rest of the Board members for their dedication and support and their advice on the issues coming before the Board.

I would also like to acknowledge and recognize the efforts and commitment of the staff throughout the year in continuing to provide our shareholders and the Board with outstanding service.

It is an honour and a privilege to continue to serve as Chair of the Alberta Capital Finance Authority and to support its continuing effort to provide our shareholders with an efficient and effective vehicle for financing of capital assets.

(original signed by)

Don Lussier
Chair

MANAGEMENT DISCUSSION AND ANALYSIS

(all amounts are cost/contractual)

The following provides management's analysis of the financial position and results of operations of the Alberta Capital Finance Authority for the year ended December 31, 2007 on a cost/contractual basis.

Loans

During 2007, the Authority loan portfolio increased from $4,903 million to $5,638 million, an increase of $735 million. New loans issued during the year totalled $1,240 million, an increase of $192 million from new loans issued in 2006 and loan repayments totalled $505 million. The Authority is forecasting that loan demand will be strong over the next few years, with increasing demands by the educational, municipal and health sectors. Included in this review is an Analysis of New Loans Issued in 2007 by Jurisdiction and Purpose, a Schedule of Loans Outstanding at December 31, 2007 and the Ten-Year Loan Review 1998-2007.

Analysis of New Loans Issued

By jurisdiction and purpose for the year ended December 31, 2007

(thousands of dollars)

	Cities	Towns	Villages	Other	Total
Sewer and water	$ 409,335	$ 11,072	$ 332	$ 21,235	$ 441,974
Transit	156,900	-	-	-	156,900
Parks and recreation	61,982	12,426	240	52,914	127,562
Electric, gas and telelphone	106,769	-	-	-	106,769
Airport Infrastructure	-	-	-	100,000	100,000
Roads and sidewalks	38,881	19,621	1,092	35,852	95,446
Student residences and ancillary operation	-	-	-	66,750	66,750
Equipment and machinery	53,928	1,754	215	3,960	59,857
Municipal buildings	18,018	10,325	165	1,350	29,858
ME *first!*	12,775	908	-	235	13,918
Landfill development	9,260	50	-	3,859	13,169
Health - ancilliary operation	-	-	-	11,308	11,308
Senior citizen lodges	5,000	807	-	5,012	10,819
Public housing	5,775	-	-	-	5,775
Land	-	200	-	-	200
Total	$ 878,623	$ 57,163	$ 2,044	$ 302,475	$ 1,240,305

Schedule of Loans Outstanding

as at December 31, 2007

(thousands of dollars)

	Principal Outstanding 31-Dec-06	2-Jan-07 to 31-Dec-07 New Loans Issued	2-Jan-07 to 31-Dec-07 Principal Repaid	Principal Outstanding 31-Dec-07
By Jurisdiction				
Cities	$2,882,659	$ 878,623	$283,304	$3,477,978
Specialized Municipalities	284,428	70,009	12,149	342,288
Towns	258,845	57,164	24,025	291,984
Villages	10,062	2,043	1,134	10,971
Counties	104,008	44,239	10,472	137,775
Municipal Districts	22,075	5,186	3,153	24,108
Irrigation Districts & Regional Services Commissions	87,665	4,983	4,536	88,112
Regional Airport Authorities	410,000	100,000	76,262	433,738
Health Authorities	135,059	11,308	7,389	138,978
Colleges, Technical Institutes & Universities	367,853	66,750	21,063	413,540
School Districts & Divisions	339,985	-	61,569	278,416
	$4,902,639	**$1,240,305**	**$505,056**	**$5,637,888**
By Purpose				
Municipal - General	$3,027,999	$ 941,560	$281,784	$3,687,775
Municipal - Utility	605,480	106,769	51,387	660,862
ME *first!*	15,568	13,918	5,239	24,247
Airport Infrastructure	410,000	100,000	76,262	433,738
Health - Ancillary Operation	135,399	11,308	7,729	138,978
Student Residence, Parkade and Ancillary Operation	367,853	66,750	21,063	413,540
School - Core Operation	340,340	-	61,592	278,748
	$4,902,639	**$1,240,305**	**$505,056**	**$5,637,888**

Ten-Year Loan Review 1998-2007

(thousands of dollars)

	2007	2006	2005
New loans issued during the year:			
By jurisdiction:			
Cities	$ 878,623	$ 619,472	$ 355,350
Specialized municipalities	70,009	159,519	6,794
Towns and villages	59,207	40,338	44,219
Counties, municipal and irrigation districts, and regional services commissions	54,408	47,806	49,656
Regional airport authorities	100,000	20,000	75,000
Health authorities	11,308	99,673	37,920
Colleges, technical institutes and universities	66,750	60,863	82,998
School districts and divisions	-	-	-
Total	**$ 1,240,305**	**$ 1,047,671**	**$ 651,937**
By purpose:			
Municipal	$ 1,048,329	$ 861,369	$ 446,841
MI *first!*	13,918	5,766	9,178
Airport infrastructure	100,000	20,000	75,000
Health – ancillary operation	11,308	99,673	37,920
Student residence, parkade and ancillary operation	66,750	60,863	82,998
School – core operation	-	-	-
Total	**$ 1,240,305**	**$ 1,047,671**	**$ 651,937**
Loans repaid during year	505,056	446,349	500,825
Loans outstanding at December 31	5,637,888	4,902,639	4,301,317
Loans outstanding at December 31 (*fair value*)	6,009,624	-	-
New debt issued during year	1,551,905	1,178,396	972,000
Debt repaid during year	835,987	570,396	832,604
Debt outstanding at December 31	5,678,476	4,963,963	4,355,963
Debt outstanding at December 31 (*fair value*)	5,929,014	-	-
Retained earnings at December 31	81,826	15,674	11,673

2004	2003	2002	2001	2000	1999	1998
$ 377,445	$ 379,647	$ 255,139	$ 297,004	$ 226,820	$ 157,516	$ 115,738
15,115	26,830	17,742	13,133	38,741	20,226	10,233
53,569	31,122	20,211	25,657	29,726	24,044	16,268
43,542	40,056	10,489	9,449	2,815	14,431	2,785
20,000	-	370,000	-	-	-	-
19,000	-	-	-	-	-	10,000
71,112	19,302	91,300	17,825	66,300	17,975	-
7,680	-	1,260	271	5,033	2,294	5,080
$ 607,463	**$ 496,957**	**$ 766,141**	**$ 363,339**	**$ 369,435**	**$ 236,486**	**$ 160,104**
$ 484,135	$ 477,655	$ 303,581	$ 345,243	$ 298,102	$ 215,967	$ 144,774
5,536	-	-	-	-	-	-
20,000	-	370,000	-	-	-	-
19,000	-	-	-	-	-	10,000
71,112	19,302	91,300	17,825	66,300	17,975	-
7,680	-	1,260	271	5,033	2,544	5,330
$ 607,463	**$ 496,957**	**$ 766,141**	**$ 363,339**	**$ 369,435**	**$ 236,486**	**$ 160,104**
397,916	410,372	418,565	456,062	427,095	422,002	562,723
4,150,205	3,940,658	3,854,073	3,506,497	3,599,220	3,656,880	3,842,396
-	-	-	-	-	-	-
714,500	3,137,000	2,280,000	725,000	592,367	-	-
475,491	2,930,523	1,929,735	776,739	1,002,367	294,206	226,645
4,216,567	3,977,558	3,771,081	3,420,816	3,472,555	3,882,555	4,176,761
-	-	-	-	-	-	-
12,664	22,406	26,676	132,738	149,913	275,656	318,602
4.923%	5.625%	5.875%	6.000%	6.125%	6.500%	5.625%

Results of Operations

The Authority's interest income on loans, including income from investments exceeded interest expense on debt by $5.8 million, as the yield on the loans was slightly higher than the yield on the debt which resulted in net income of $5.2 million after other revenue and expenses. With the change to fair value accounting, net income was increased to $8.4 million after the unrealized gains and losses from loans, debt and derivatives were accounted for.

The Authority's goals are to provide local authorities with flexible funding at the lowest possible cost and to maintain the lowest administrative and new loan costs compared to other municipal borrowing authorities. Included below is a comparison of the Authority's 2007 costs with the March 31, 2007 audited financial data of other provincial municipal borrowing authorities.

Capital Finance Authority Statistics - 2007

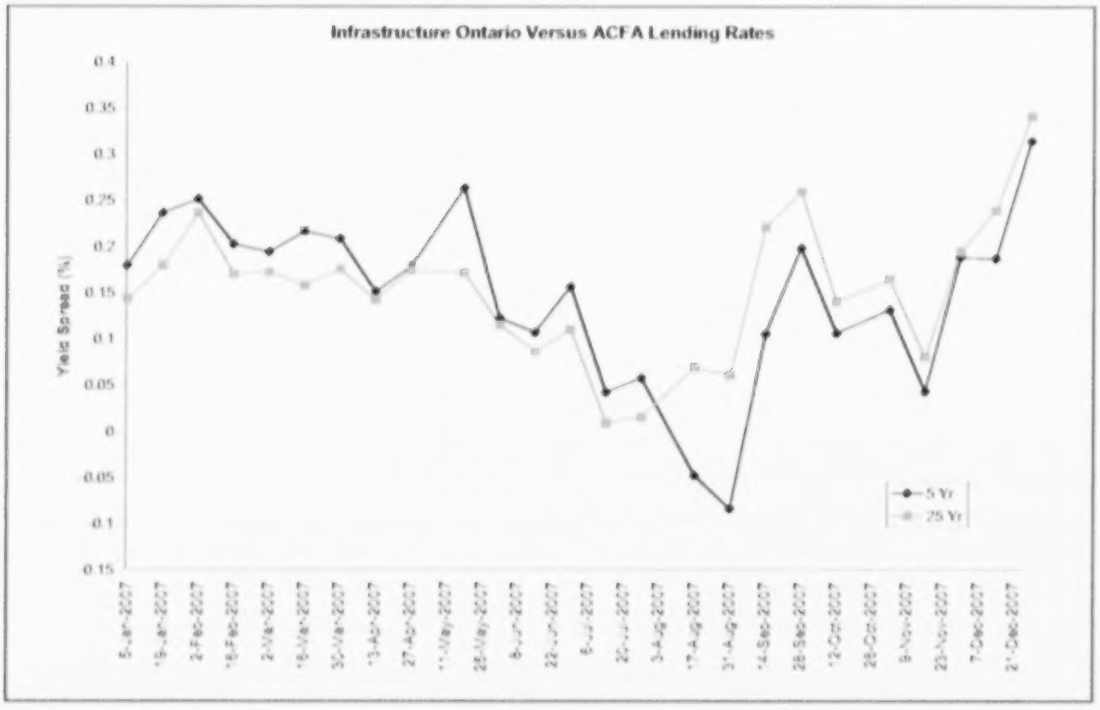
	Alberta	British Columbia	Nova Scotia
New loans to shareholders *($ millions)*	1,240	613	108
Total loans outstanding, net of unamortized discounts *($ millions)*	5,636	3,573	642
Administrative expense			
($ thousands)	659	1,297	379
($ per $ thousand of new loans)	.53	2.12	3.51
($ per $ million of loans)	.12	.36	.59

Interest Rates

The Authority provides fixed rate semi-annual pay amortizing loans to its borrowers. Loan rates are based on actual rates for the interest rate swaps (or other floating rate instruments) executed to convert the loan to a floating rate to match the funding floating rate in order to reduce interest rate risk to the Authority. If a fixed rate instrument is used to fund the loan, then the loan rate will be based on the actual rate of the fixed rate instrument.

Comparative Loan Spreads with Infrastructure Ontario

In order to compare the Authority's loan rates provided to those of Ontario municipal borrowers, rates of Infrastructure Ontario were reviewed and compared to the rate that the Authority would have offered. As noted below ACFA's rates were consistently below Infrastructure Ontario's throughout the year except for August when Infrastructure Ontario's rates were 8 basis points below ACFA's rate. Spreads between ACFA's rates and Infrastructure Ontario's rates remained constant between 15 and 25 basis points for the first part of the year, declined to 3 to minus 8 basis points in August and increased to 30 and 35 basis points by the end of the year. The Authority's goal is to provide the lowest rate for Alberta borrowers.



Debt

The gross debt of the Authority increased by $715 million to $5,679 million. During the year, the Authority received $505 million in loan repayments while issuing $1,240 million in new loans. The Authority repaid $335 million to the Canada Pension Plan Investment Fund. During the year the Authority borrowed $1,010 million in medium and long-term debt for terms from 3 to 25-years and to meet short-term requirements, borrowed over $542 million, of which $502 million was repaid during the year.

Sources of Capital
(thousands of dollars)

	Contractual Outstanding 31-Dec-07	Outstanding as a Percentage of Total
Canada Pension Plan	$1,705,963	30%
Public	3,972,513	70%
Total	$5,678,476	100%

Risk Management

Effective risk management is central to the ability to ensure a financially sound organization and includes identifying, assessing, managing and monitoring all forms of risk. The Authority is primarily exposed to:

- Market risk
- Liquidity risk
- Operational risk and
- Credit risk

The President of the Authority is responsible for identifying risks and recommending the appropriate policies and framework. The Board of Directors reviews and approves the risk management policies and implements specific reporting procedures to enable them to monitor the adherence to these policies.

Market Risk

Market risk is the impact on the Authority's income from changes in market factors such as interest rates and foreign exchange. The Authority requires that all borrowing be done in Canadian dollars or that borrowing in foreign currency be swapped into Canadian dollars. The primary source of interest rate risk is repricing risk which arises when there is a mismatch between the maturity and repricing of interest bearing assets and liabilities. This repricing risk also results from the Authority's willingness to allow for some prepayments on existing loans.

The prepayment policy is structured to protect the Authority from the significant losses that would occur in accepting additional prepayments of high interest rate loans and relending these funds at lower rates. The Authority, on three separate occasions, has reduced the rates on higher interest rate loans to 12%. The Authority does not have the ability to prepay or refinance its public debt and can only repay the Canada Pension Plan Investment Fund with a prepayment penalty based on current market rates which would not make it economically advantageous. The Authority's prepayment policy is an integral part of its long-term financial planning.

Interest Rate Risk

The Authority uses mainly interest rate swaps for the purpose of managing its asset and liability position. The Authority's policy is to match the interest rate exposure on all new loans to the interest rate exposure of the debt used to fund these loans. In most cases, fixed interest rates on new loans and debt are swapped to floating rates so that the rates on both loans and debt are equal.

The Board recognizes the unique risks associated with the use of derivative financial instruments and has established policies and procedures to monitor and minimize exposure to the Authority. These policies and procedures limit the type of derivative financial instruments and circumstances where they can be used, the authorities required to approve the transaction and the appropriate segregation of duties to reduce operational risk. All derivative financial instruments are reviewed and managed within policies approved by the Board and the Board reviews all derivative financial instruments acquired since the last meeting.

Credit risk on counterparty default arises with the use of derivatives. To control this risk, the Authority uses counterparty limits established for the Province and uses only counterparties believed to have a good credit standing (A+ or greater). The Authority is not exposed to credit risk for the full face value (notional amount) of the derivative contracts, but only to the potential replacement cost if the counterparties fail. This exposure is represented by the current replacement cost of all outstanding contracts in a favourable position. For additional information, see Note 6 in the Financial Statements.

Liquidity Risk

Liquidity risk is the risk that the Authority will not have sufficient cash to meet its obligations as they become due and also meet the loan requirements of our local authorities.

The Authority manages its liquidity risk by monitoring its cash flows on a daily basis and providing updated cash flow reports to the Board as required. Surplus funds are invested short-term in the Consolidated Cash Investment Trust Fund. When required, the Authority raises funds under a five-year Promissory Note Program, by direct borrowing in the Canadian or European market or by renewing borrowing from the Canada Pension Plan.

Operational Risk

Operational risk is the risk associated with a breakdown in internal controls, systems or procedural failures, human errors or malfeasance. These risks can never be fully eliminated but are minimized by establishing appropriate policies and sound internal controls through an appropriate segregation of duties, accountability and reporting practices.

The audit of the financial statements was made in accordance with Canadian generally accepted auditing standards and, accordingly, included a review of certain of the systems of operating and financial controls and such tests that were considered necessary in the circumstances.

The objective of a financial statement audit is to obtain reasonable assurance whether the financial statements are free of material misstatement. Accordingly, an audit would not usually identify all matters that may be of interest to management and the Audit Committee, however any weaknesses identified in internal controls over financial reporting controls, or other non-trivial matters, are communicated to management and the Audit Committee.

Credit Risk

Credit risk is the risk of loss due to a borrower failing to meet their obligations to the Authority. Historically, the Authority has not been required to record any provisions or allowances regarding credit losses nor has it suffered any such losses. The Authority has established policies which provide for the approval and monitoring of all lending activity. These policies include establishing clear lines of authority for decision making and for accountability.

ALBERTA CAPITAL FINANCE AUTHORITY

Financial Reporting Responsibility of Management

Management of the Alberta Capital Finance Authority prepared these financial statements and is responsible for their reliability, completeness and integrity. They conform in all material respects to Canadian generally accepted accounting principles and the requirements of the *Alberta Capital Finance Authority Act*.

Management maintains the necessary accounting and internal control systems designed to ensure the timely production of reliable and accurate financial information, the protection of assets (to a reasonable extent) against loss or unauthorized use and the promotion of operational efficiency. The Audit Committee oversees management's responsibilities for financial reporting, and internal control systems over financial reporting controls, and recommends approval of the financial statements and annual report to the Board of Directors.

The Auditor General of Alberta is designated as the external auditor in the *Alberta Capital Finance Authority Act*. The Audit Committee reviewed these financial statements with the external auditor in detail before recommending their approval to the Board of Directors. The Board then approved the financial statements.

(original signed by)

T. S. Stroich

FCA
President

Edmonton, Alberta
February 7, 2008

OFFICE OF THE AUDITOR GENERAL

Auditor's Report

To the Shareholders of the Alberta Capital Finance Authority

I have audited the balance sheet of the Alberta Capital Finance Authority as at December 31, 2007 and the statement of net income, comprehensive income and retained earnings and cash flow for the year then ended. These financial statements are the responsibility of the Authority's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with Canadian generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Authority as at December 31, 2007 and the results of its operations and its cash flows for the year then ended in accordance with Canadian generally accepted accounting principles.

(original signed by)

Fred J. Dunn

FCA
Auditor General

Edmonton, Alberta
February 7, 2008

BALANCE SHEET

as at December 31, 2007
(thousands of dollars)

	2007	2006 (Note 2a)
Assets:		
Cash (Note 3)	$ 16,272	$ 20,800
Accrued interest receivable	-	103,245
Loans to local authorities (Note 4)	6,009,624	4,898,705
Derivatives in favourable position (Note 6)	50,230	-
	$ 6,076,126	$ 5,022,750
Liabilities and Shareholders' Equity:		
Liabilities:		
Accounts payable	$ 733	$ 741
Accrued interest payable	-	56,086
Debt (Note 5)	5,929,014	4,950,185
Derivatives in unfavourable position (Note 6)	64,489	-
	5,994,236	5,007,012
Shareholders' equity:		
Share capital (Note 7)		
Issued and fully paid:		
6,390 shares	64	64
Retained earnings (Note 2a)	81,826	15,674
	81,890	15,738
	$ 6,076,126	$ 5,022,750

The accompanying notes are part of these financial statements

(original signed by)

D.O. Lussier
Chair of the Board

(original signed by)

T.S. Stroich, FCA
President

Statement of Net Income, Comprehensive Income and Retained Earnings

for the year ended December 31, 2007

(thousands of dollars)

	Budget (Note 11)	2007 (Note 2a)	2006 (Note 2a)
Interest Income:			
Loans	$ 292,078	$ 307,432	$ 284,849
Amortization of loan discounts	2,282	-	4,027
Investments (Note 3)	7,400	4,359	5,517
	301,760	311,791	294,393
Interest Expense:			
Debt	293,031	301,763	290,082
Commission fees	-	4,200	-
Amortization of net discounts on debt	1,428	-	1,556
	294,459	305,963	291,638
Net interest income	7,301	5,828	2,755
Other Income:			
Loan prepayment fees	-	58	2,127
Net interest income and other income	7,301	5,886	4,882
Non-Interest Expense:			
Administration and office expenses (Note 8)	705	659	881
Income before unrealized gains (losses)	6,596	5,227	4,001
Unrealized loss on loans	-	(65,954)	-
Unrealized gain on debt	-	73,210	-
Unrealized loss on derivatives	-	(4,074)	-
Total unrealized gain	-	3,182	-
Net income and comprehensive income (Note 2d)	6,596	8,409	4,001
Retained earnings, beginning of year (Note 2a)	16,051	73,417	11,673
Retained earnings, end of year	$ 22,647	$ 81,826	$ 15,674

Statement of Cash Flow

for the year ended December 31, 2007
(thousands of dollars)

	2007	2006 (Note 2a)
Operating Activities:		
Interest received	$ 310,252	$ 291,266
Investment interest	4,359	5,517
Loan prepayment fees	58	2,127
Commission fees	(4,200)	-
Administration and office expenses	(559)	(881)
Interest paid	(295,107)	(287,006)
Cash flows from operating activities	14,803	11,023
Investing Activities:		
Loan repayments	505,056	446,349
New loans issued	(1,240,305)	(1,047,671)
Cash flows used in investing activities	(735,249)	(601,322)
Financing Activities:		
Debt issues	1,551,905	1,171,191
Debt redemptions	(835,987)	(570,396)
Cash flows from financing activities	715,918	600,795
Net (decrease) increase in cash	(4,528)	10,496
Cash, beginning of year	20,800	10,304
Cash, end of year	$ 16,272	$ 20,800

Notes to the Financial Statements

December 31, 2007
(all amounts presented in thousands of dollars, except share amounts)

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1. **Authority**

   The Alberta Capital Finance Authority (ACFA) operates under the authority of the *Alberta Capital Finance Authority Act*, Chapter A-14.5, Revised Statutes of Alberta 2000, as amended. Under the Act, the Authority is restricted to making loans only to its shareholders.

2. **Significant Accounting Policies and Reporting Practices**

   These financial statements have been prepared by management in accordance with Canadian Generally Accepted Accounting Principles (GAAP) and include the following changes to/and significant accounting policies:

   a) **Changes in Accounting Policies**

      Effective January 1, 2007, ACFA adopted new or revised accounting standards issued by the Canadian Institute of Chartered Accountants (CICA): CICA Handbook Section 1530, Comprehensive Income; Section 3855, Financial Instruments – Recognition and Measurement; Section 3861; Financial Instruments – Disclosure and Presentation; Section 3865, Hedges. The adoption of new accounting policies to comply with these standards, often collectively referred to as "the financial instruments standards" or "the new standards", resulted in certain changes to ACFA accounting for financial instruments and hedges. As these new policies have been adopted prospectively, prior period results have not been restated and certain transition adjustments have been recorded in opening retained earnings as of January 1, 2007.

      Prior to adopting the new standards, ACFA accounted for virtually all of its financial assets (principally cash resources and loans) and financial liabilities (principally long-term debt) on an accrual basis and measured them at cost or amortized cost, as applicable. ACFA's derivative contracts that qualified for hedge accounting were accounted for on an accrual basis. Income and expenses on derivative financial instruments designated and qualifying as hedges were recorded as an adjustment to the yield of the item being hedged over the term of the hedge contract in the Statement of Net Income, Comprehensive Income and Retained Earnings. The fair values of the derivative contracts were not recorded on the Balance Sheet during the life of the hedging relationship. Accrued interest receivable and payable on these derivative financial instruments were recorded in accrued interest receivable and payable respectively, in the Balance Sheet.

      Section 3855 establishes a framework for the recognition and measurement of financial assets, financial liabilities, and non-financial derivatives. All existing financial instruments have been classified as held for trading as of January 1, 2007 according to this new framework. Any new financial instruments entered into after that date will be classified on inception and will be recorded on the Balance Sheet at fair value. All previously designated hedging relationships have been voluntarily de-designated.

      Changes in fair value (realized or unrealized gains or losses) of financial assets and liabilities are recorded in net income in the Statement of Net Income, Comprehensive Income and Retained Earnings. Any interest earned (or incurred) continues to be recognized on an accrual basis as interest income (or expense).

The new standards for financial instruments require all derivative financial instruments, including embedded derivatives, to be classified as held-for-trading and measured at fair value on the Balance Sheet beginning January 1, 2007. Derivatives having positive fair value are presented as derivative assets and those having negative fair value are presented as derivative liabilities. Changes in the fair value of derivative financial instruments are now recorded in net income.

Transaction costs related to held for trading financial instruments are expensed as incurred. Prior to January 1, 2007, transaction costs (syndicate commissions) related to the issuance of debt were amortized on a straight line basis therefore an adjustment of $7,202 was made to opening retained earnings to recognize the unamortized portion of these costs.

On ACFA's adoption of new accounting policies for financial instruments, the following transition adjustments have been recorded as adjustments to the opening January 1, 2007 balances of assets, liabilities and retained earnings:

		31-Dec-06	
	Cost	**Fair Value**	**Adjustment**
Assets			
Loans, including accrued interest	$5,001,950	$5,343,149	$341,199
Derivative instruments	-	38,943	38,943
			380,142
Liabilities			
Debt, including accrued interest	$5,006,271	$5,279,542	$273,271
Derivative instruments	-	49,128	49,128
			322,399
Cumulative impact of adopting the financial instruments standards			57,743
Retained earnings, beginning of year, as issued			15,674
Retained earnings, beginning of year, restated			$73,417

b) Future Accounting Changes

The following summarizes future accounting changes that will be relevant to ACFA's financial statements subsequent to January 1, 2008.

Capital Disclosures

The CICA has issued a new accounting standard Section 1535, Capital Disclosures that establishes requirements for Capital Disclosures. This will be effective for ACFA commencing January 1, 2008 and requires disclosure of an entity's objectives, policies and processes for managing capital, quantitative data about what is considered capital and whether an entity has complied with any capital requirements and consequences of non-compliance with such capital requirements.

Financial Instruments – Disclosure

The CICA has issued two new accounting standards Section 3862, Financial Instruments – Disclosures and Section 3863, Financial Instruments – Presentation on Financial Instruments that revise and enhance the current disclosure requirements but do not change the existing presentation requirements for financial instruments. These new standards will be effective for ACFA commencing January 1, 2008. The new disclosures will provide additional information on the nature and extent of risks arising from financial instruments to which ACFA is exposed and how it manages those risks.

c) Measurement Uncertainty

The preparation of financial statements in conformity with Canadian GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of revenues and expenses during the year. Actual results could differ from these estimates. Measurement uncertainty exists in the collectability of the loans to local authorities and the estimate of fair value of financial instruments.

d) Comprehensive Income

Comprehensive income is composed of net income and other comprehensive income. Other comprehensive income may include any unrealized gains and losses on available-for-sale securities and changes in the fair market value of derivative instruments designated as cash flow hedges. As ACFA did not have any elements of other comprehensive income at January 1, 2007 or December 31, 2007, the adoption of this section did not have an impact on the financial statements.

3. Cash

Cash is on deposit in the Consolidated Cash Investment Trust Fund of the Province of Alberta which is managed with the objective of providing competitive interest income to depositors while maintaining appropriate security and liquidity of depositors' capital. The portfolio is comprised of high-quality short-term and mid-term fixed-income securities with a maximum term-to-maturity of three years. As at December 31, 2007, securities held by the Fund have an average net return of 4.48% per annum (December 31, 2006 – 4.55% per annum).

The fair value of cash approximates its carrying value.

4. Loans to Local Authorities

Loans to Local Authorities	2007	2006
Fair value	$6,009,624	$5,343,149
Contractual principal	$5,637,888	$4,902,639
Unamortized discount	(1,652)	(3,934)
Accrued interest receivable	100,425	103,245
	$5,736,661	$5,001,950

The fair values of loans are calculated using future interest and principal cash flows for all loans using a discount factor curve to determine the present value of each cash flow.

The discount factor curve is calculated using the ACFA's estimated market borrowing rates as a base and adding a premium of 12 basis points to this curve. ACFA's borrowing rates are used as a base as it is assumed based on payment history and security covenants in place, that the loan portfolio has credit risk similar to that of ACFA. The premium of 12 basis points is added to these rates as it is expected that financial securities with irregular payments would require a higher rate if sold in the market. The premium was determined through analysis of premiums for amortizing bonds trading in the bond market. The estimated sensitivity of the fair value of loans to a change in the discount factor of one (1) basis point is $3,803.

Credit risk is the risk of loss due to borrowers failing to meet their obligations to ACFA. Historically, ACFA has not needed to record any provisions or allowances regarding credit losses nor has it suffered any such losses. ACFA has established policies which provide for the approval and monitoring of all lending activity. These policies include establishing clear lines of authority for decision making and for accountability.

5. Debt

Debt (Schedule 1)	2007	2006
Fair Value	$5,929,014	$5,279,542
Contractual principal	$5,678,476	$4,963,963
Unamortized discount	(12,373)	(13,778)
Accrued interest payable	62,850	56,086
	$5,728,953	$5,006,271

Market rates for ACFA debt are based on credit spread indications for new debt issues received from ACFA's borrowing syndicate managers and are determined by taking Government of Canada bond interest rates at the close of business on the last business day of the period and adding the indicative new issue spread to these rates. The estimated sensitivity of the fair value of debt to a change of one (1) basis point in the rate used to calculate fair value is $3,832.

Bonds (i.e. bullets with no options with the entire principal amount paid at maturity) are valued by interpolating the yield to maturity for each individual bond from the calculated indicative borrowing rates. This yield to maturity is used to calculate the market value, including accrued interest, for each bullet bond using common bond pricing methodology.

Structured notes, including step-up notes and accrual notes, are valued using formulas that require a discount factor curve, which is computed from the indicative borrowing rates and inputs on option volatility as estimated in the swap market.

The debt of ACFA is fully guaranteed by the Province of Alberta.

Debt amounting to $762,513 (2006 - $643,000) is comprised of a combination of various issues of step-up and accrual notes whereby ACFA has the option of extending or calling the debt, at predetermined extension or call dates. Principal is due upon termination of the debt, where debt is called or not extended by ACFA at the predetermined extension or call date, or upon final maturity of the debt (Schedule 1).

For the next five years contractual debt redemption requirements, with the assumption that the step-up and accrual notes are redeemed at the first extendible date and all other debt at the maturity date, are as follows:

	Debt Redemption
2008	$1,049,807
2009	330,523
2010	212,000
2011	250,000
2012	500,000
	$2,342,330

6. Derivative Financial Instruments

Derivative financial instruments used by ACFA include interest rate swaps and forward rate agreements.

The interest rate contracts are used to manage exposure to fluctuations in interest rates in certain fixed rate loans and debt made after January 1, 2004.

Notional amounts represent the amount to which a rate is applied in order to calculate the exchange of cash flows. The notional amounts are not recorded in the Balance Sheet. They represent the volume of outstanding transactions and do not represent the potential gain or loss associated with the market risk or credit risk of such instruments.

The notional amounts of derivative financial instruments are summarized as follows:

	As at December 31					
Maturities	**Within 1 Year**	**1 to 2 Years**	**3 to 5 Years**	**6 to 10 Years**	**Over 10 Years**	**Total**
Interest rate swaps - 2007	$1,450,216	$ 14,154	$ 220,360	$1,061,787	$3,716,037	$6,462,554
Interest rate swaps - 2006	$ 652,290	$ 639	$ 181,175	$ 976,856	$2,516,099	$4,327,059

The cost of replacing the remaining cash flows of the derivative financial instruments at the prevailing prices and market rates are summarized as follows:

			Current Replacement Cost	
	Notional Outstanding	**Net Fair Value**	**Contracts in Favourable Position**	**Contracts in Unfavourable Position**
Interest rate swaps - 2007	$ 6,462,554	$ (14,259)	$ 50,230	$ (64,489)
Interest rate swaps - 2006	$ 4,327,059	$ (10,185)	$ 38,943	$ (49,128)

Fair values are determined using models based on third party valuation software which takes into account current market and contractual prices of the underlying instruments, as well as time value and yield curve or volatility factors underlying the positions. Fair values have been segregated between those contracts which are in a favourable position (positive fair value) and those contracts which are in an unfavourable position (negative fair value) and are recorded as derivative assets and derivative liabilities respectively. Changes in the fair value of derivative instruments are now recorded in income. The estimated sensitivity of the fair value of derivatives in a favourable and unfavourable position to a change in the rate of one (1) basis point is $798 and $690 respectively.

Current credit exposure is limited to the amount of loss that ACFA would suffer if every counterparty to which ACFA was exposed were to default at once and is represented by the current replacement cost of all outstanding contracts in a favourable position. ACFA actively monitors their exposure and minimizes credit risk by only dealing with counterparties believed to have a good credit standing (A+ or greater).

7. **Share Capital**

Particulars of share capital are as follows:

			Number of Shares		
Class	**Restricted to**		**Authorized**	**Issued and Fully Paid**	**Total Dollar Amount**
A	Province of Alberta		4,500	4,500	$45,000
B	Municipal authorities, airport and health authorities		1,000	874	8,740
C	Cities		750	585	5,850
D	Towns and villages		750	294	2,940
E	Educational authorities		500	137	1,370
		2007	7,500	6,390	$63,900
		2006	7,500	6,384	$63,840

During the year, nine Class B shares were issued and three Class D shares were cancelled at $10.00 each.

8. **Directors' and Audit Committee Fees and Related Party Transactions**

Directors' and Audit Committee fees paid by the Authority are as follows:

	2007		2006	
	Number of Individuals	**Total**	**Number of Individuals**	**Total**
Board/Audit Committee Chairs	2	$ 8	2	$ 7
Board/Audit Committee members	8	$ 19	8	$ 20

There are two additional Board members who are employees of the Province of Alberta and do not receive compensation from ACFA.

ACFA has advanced loans to local authorities under the ME*first!* Municipal Energy Efficiency Assistance Program (the "Program") on behalf of Alberta Municipal Affairs and Housing and Alberta Environment. Under the Program, principal was advanced to qualifying municipalities by ACFA and repayments of principal are made by the municipality; however, the interest is paid by the Province of Alberta. The Program has been discontinued but the loans will continue until they are paid out. Included in the balance of loans to local authorities at December 31, 2007 is principal of $24,247 (2006 - $15,568), upon which, interest of $959 (2006 - $560) has been recorded in interest income from loans.

ACFA has no employees. Included in administration and office expenses of $659 (2006 - $881) is the amount of $420 (2006 - $406) that was paid to the controlling shareholder, Province of Alberta for services at prices measured at the exchange amount, which approximate market.

9. Interest Rate Risk

Interest rate risk refers to the potential impact of changes in interest rates on ACFA's earnings when maturities of its financial assets are not matched with the maturities of its financial debt. The following table summarizes the contractual principal amounts of ACFA's interest sensitive assets and liabilities based on the earlier of repricing or principal repayments:

As at December 31

Maturities	Within 1 Year	1 to 2 Years	3 to 5 Years	6 to 10 Years	Over 10 Years	2007 Total	2006 Total
Assets							
Cash	$ 16,272	$ -	$ -	$ -	$ -	$ 16,272	$ 20,800
Accrued Interest Receivable	100,425	-	-	-	-	100,425	103,245
Loans to Local Authorities	419,583	563,406	1,155,027	1,459,632	2,040,240	5,637,888	4,902,639
Effective Rate	5.9%	6.0%	5.6%	5.4%	5.2%	5.6%	6.0%
Total	$ 536,280	$ 563,406	$1,155,027	$1,459,632	$2,040,240	$5,754,585	$5,026,684
Liabilities							
Accrued Interest Payable	$ 62,850	$ -	$ -	$ -	$ -	$ 62,850	$ 56,086
Debt	1,049,807	330,523	962,000	1,800,000	1,536,146	5,678,476	4,963,963
Effective Rate	6.2%	5.5%	5.2%	5.3%	5.5%	5.5%	5.7%
Total	$1,112,657	$ 330,523	$ 962,000	$1,800,000	$1,536,146	$5,741,326	$5,020,049
Cumulative Gap	$ (576,377)	$ 232,883	$ 193,027	$ (340,368)	$ 504,094	$ 13,259	$ 6,635

ACFA manages its interest rate risk by matching its debt maturity profile to the forecast cash flows and their effect on ACFA's surplus position. For most loans made after January 1, 2004, ACFA uses derivative financial instruments to swap fixed rate loans interest to floating, and swap corresponding debt from fixed rate to floating and uses forward rate agreements to minimize the exposure related to the mismatch of reset dates of the loan and debt swaps.

Liquidity Risk

Liquidity risk is the risk that ACFA will not have sufficient cash to meet its obligations as they become due and also meet the loan requirements of our local authorities.

ACFA manages its liquidity risk by monitoring its cash flows on a daily basis. Surplus funds are invested in short-term investments or the Consolidated Cash Investment Trust Fund. When required, ACFA raises funds under a five-year Promissory Note Program, by direct borrowing in the Canadian or European market or by renewing borrowing from the Canada Pension Plan Investment Board.

10. Commitments Lease

ACFA has obligations under an operating lease for the rental of premises, expiring in July 2013 at an annual minimum as follows:

2008 – $37
2009 – $50
2010 – $53
2011 – $54
2012 – $54

Loan Commitments

In the normal course of business, ACFA enters into loan commitments to provide customers with sources of credit.

Commitments to extend credit represent undertakings to make credit available in the form of loans for specific amounts and maturities, subject to certain conditions and are recently authorized loans not yet drawn down.

These loan arrangements are subject to ACFA's normal credit standards and collateral is obtained where appropriate. The loan amounts represent the maximum credit risk exposure to ACFA should the loans be fully drawn. The loan commitments represent future cash requirements and as at December 31 were:

	2007	2006
Loan commitments as at December 31	$ 11,000	$ 30,308

Debt Commitments

In the normal course of business, ACFA enters into debt commitments to insure ACFA obtains the necessary funds to make loans. These transactions may occur over the year end with the trading date prior to and the settlement date after the year end.

The commitments as at December 31 were:

	2007	2006
Debt commitments as at December 31	$ 13,000	$ -

Proceeds of $13,000 from the 4.45% step-up note extendible at ACFA's option were received on January 4, 2008.

11. Budget

The 2007 budget was approved by the Board of Directors on November 23, 2006.

12. Comparative Figures

Certain comparative figures have been reclassified to conform to the current year's presentation.

SCHEDULE OF DEBT

As at December 31, 2007 — Schedule 1

(thousands of dollars)

Maturity Date	First Extendible Date	Interest Rate	Contractual Principal Outstanding	Fair Value	
Canada Pension Plan Investment Fund/CPP Investment Board					
Oct 03, 2008		10.040	$259,294	$277,307	
Oct 02, 2009		9.990	291,414	327,818	
Nov 01, 2009		9.620	32,457	36,155	
Dec 01, 2009		9.260	6,652	7,339	
Oct 01, 2020		6.280	222,367	263,870	
Jun 01, 2022		6.060	100,000	116,540	
Apr 05, 2023		5.890	50,000	58,042	
Dec 01, 2023		5.500	150,000	166,705	
Dec 03, 2024		5.180	78,000	84,006	
Nov 03, 2026		4.490	200,000	199,409	
Nov 03, 2031		4.500	125,396	124,822	
Nov 02, 2032		4.830	190,383	198,818	
Total			1,705,963	1,860,831	
Public					
Jan 04, 2008		3.860	20,000	19,990	
Feb 01, 2008		3.860	20,000	19,921	
Mar 24, 2008	Mar 24, 2008	4.000	16,000	16,486	(i)
Mar 01, 2010		4.550	50,000	51,258	
Jun 15, 2010	Jun 15, 2008	4.400	10,000	10,198	(i)
Aug 20, 2010		4.500	150,000	153,879	
Nov 23, 2010	Nov 23, 2008	4.500	10,000	10,004	(i)
Jun 23, 2011	Jun 23, 2008	3.350	10,000	10,005	(i)
Sep 01, 2011		5.700	200,000	213,907	
Sep 06, 2011	Mar 06, 2008	4.350	10,000	10,045	(i)
Sep 11, 2011	Mar 11, 2008	4.350	20,000	20,078	(i)
Sep 15, 2011	Mar 15, 2008	3.600	10,000	9,903	(i)
Dec 15, 2011		4.435	50,000	50,508	
Dec 15, 2011	Jun 15, 2008	3.600	13,000	12,744	(i)
Mar 30, 2012	Mar 30, 2008	4.050	10,000	10,149	(i)
May 11, 2012	May 11, 2008	4.000	10,000	9,937	(i)
Jun 01, 2012		5.850	500,000	534,756	
Aug 28, 2012	Feb 28, 2008	4.400	10,000	10,052	(i)
Jun 28, 2013	Jun 28, 2008	3.750	15,000	14,637	(i)
Oct 12, 2013	Apr 12, 2008	3.750	10,000	9,855	(i)
Oct 30, 2013	Apr 30, 2008	4.300	10,000	9,905	(i)
Nov 20, 2013	Nov 20, 2008	4.600	10,000	9,945	(i)
Dec 02, 2013		5.000	300,000	312,040	
Oct 22, 2014	Oct 22, 2008	4.800	10,000	9,995	(i)
Dec 15, 2014	Jun 15, 2008	4.750	25,000	24,864	(i)
Dec 15, 2014	Jun 15, 2008	4.600	30,000	29,740	(i)
Mar 23, 2015	Mar 23, 2008	4.450	20,000	22,210	(ii)
Mar 30, 2015	Mar 30, 2008	4.150	15,000	15,200	(i)
Apr 06, 2015	Apr 06, 2008	4.250	15,000	14,868	(i)

Maturity Date	First Extendible Date	Interest Rate	Contractual Principal Outstanding	Fair Value	
Jun 01, 2015		4.900	200,000	207,453	
Jun 15, 2015	Jun 15, 2008	4.050	10,000	9,962	(i)
Jun 15, 2015	Jun 15, 2008	4.200	45,000	44,081	(i)
Jun 15, 2015	Jun 15, 2008	4.050	17,000	16,871	(i)
Jun 15, 2015	Jun 15, 2008	3.450	15,000	14,495	(i)
Jun 23, 2015	Jun 23, 2008	3.800	15,000	15,884	(ii)
Jun 28, 2015	Jun 28, 2008	4.300	20,000	21,550	(ii)
Sep 15, 2015	Mar 15, 2008	4.240	10,000	10,610	(ii)
Dec 15, 2015	Jun 15, 2008	4.200	20,000	19,469	(i)
Jun 15, 2016	Jun 15, 2008	4.050	25,000	24,286	(i)
Jun 15, 2016		4.350	600,000	598,908	
Mar 15, 2017	Mar 15, 2008	4.715	15,513	15,140	(ii)
Apr 10, 2017	Apr 10, 2008	4.350	15,000	14,751	(i)
May 15, 2017	Mar 15, 2008	4.150	25,000	24,502	(i)
Jun 15, 2017		4.650	700,000	712,934	
Jun 16, 2017	Jun 16, 2008	4.200	18,000	17,551	(i)
Jun 28, 2017	Jun 28, 2008	4.100	30,000	28,912	(i)
Aug 15, 2017	Feb 15, 2008	4.100	35,000	34,341	(i)
Dec 15, 2017	Jun 15, 2008	4.100	10,000	9,713	(i)
Jun 01, 2018		5.150	100,000	106,119	
Nov 16, 2018	May 16, 2008	4.650	18,000	17,740	(i)
Nov 13, 2020	Nov 13, 2008	5.020	12,000	11,705	(ii)
Apr 18, 2022	Apr 18, 2010	5.000	12,000	12,085	(ii)
Jun 15, 2022	Jun 15, 2008	5.010	25,000	25,077	(ii)
Dec 01, 2023		5.100	20,000	21,322	
Jun 15, 2025	Jun 15, 2008	5.150	20,000	22,342	(ii)
Jul 06, 2025	Jan 06, 2008	5.020	16,000	17,603	(ii)
Dec 15, 2025		4.450	300,000	296,418	
Oct 11, 2030	Oct 11, 2008	5.160	15,000	16,049	(ii)
Dec 15, 2030	Jun 15, 2008	5.160	10,000	10,908	(ii)
Dec 15, 2030	Dec 15, 2008	5.410	10,000	11,242	(ii)
Dec 15, 2030	Jun 15, 2008	5.400	10,000	11,081	(ii)
Total			3,972,513	4,068,183	
Total debt 2007			$5,678,476	$5,929,014	
Total debt 2006			$4,963,963	$5,279,542	

(i) These are step-up notes extendible at the ACFA's option which pay interest periodically at a predetermined rate with principal paid on termination.

(ii) These are accrual notes extendible or callable at the ACFA's option which accrue interest compounded semi-annually or annually, and pay interest and principal on termination.